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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	WT Docket No. 97-82
Amendment of Part 1 of the	)	
Commission's Rules --	)	
Competitive Bidding Proceeding	)	
	)	

To: The Commission

ORIGINAL

COMMENTS OF POCKET COMMUNICATIONS, INC.

By: William R. Richardson, Jr.
Lynn R. Charytan
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037
(202) 663-6000

SUMMARY

Pocket Communications, Inc., the parent company of a PCS C block licensee, supports the Commission's efforts to amend and clarify its auction rules. The auction rules have provided small businesses with an unprecedented opportunity to enter the wireless telecommunications market. However, some of the rules have unintentionally made it more rather than less difficult for small businesses to raise the capital they need in order to build out their systems and compete with existing services. Many small business licensees are start-up telecommunications businesses that will not earn revenues during the first few years of their license terms while they build out their markets and implement their business plans. Clarification or amendment of some of the Commission's rules to reflect this situation would assist not only prospective but existing small business licensees, especially those in the C block.

TABLE OF CONTENTS

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COMMENTS OF POCKET COMMUNICATIONS, INC.

Pocket Communications, Inc. ("Pocket") respectfully submits these comments in response to the Notice of Proposed Rulemaking ("NPRM") in the above-captioned matter. As the parent company of a C block PCS licensee, Pocket has had substantial experience with the effect of the Commission's competitive bidding rules on the ability of small businesses to compete in spectrum auctions, and to attract the capital that is necessary to build out and operate successful wireless systems. The Commission's rules to date have been enormously helpful in providing small businesses with an opportunity -- that otherwise would have been entirely unavailable -- to enter the market for broadband wireless services. Both prospective license applicants and existing C block licensees (and other small business licensees) stand to benefit even further from some fine tuning of those rules in order to clarify and simplify certain issues that, in some cases, have complicated licensees' efforts to raise funds.

I. THE FINANCIAL ATTRIBUTION RULES SHOULD BE SIMPLIFIED FOR ALL LICENSEES TO FACILITATE EFFORTS TO ATTRACT INVESTMENT.

The Commission's broadband PCS rules require that small business licensees have a "control group" with certain minimum fully diluted equity percentages, and attribute the gross revenues of all control group members and their affiliates, and other investors that, together with their affiliates, have more than 25% (in most cases) of the fully diluted equity or voting control. See, e.g. 47 C.F.R. § 24.709(b)(3). The Commission's suggested change, which would involve attributing the revenues only of the principals who exercise de jure and de facto control (and their affiliates), NPRM ¶ 28, and thus dispensing with the control group rules and nonattributable equity caps, would be simpler to implement and would help facilitate efforts to raise capital. Indeed, the Commission has concluded as much in other contexts where it has abandoned the control group rules entirely in favor of the more general control approach. See, e.g., Second Report and Order, Order on Reconsideration, and Fifth Notice of Proposed Rulemaking, FCC 97-82, ¶ 352 (released March 13, 1997) (control group rules not adopted for LMDS). Moreover, the Commission should adopt its new proposed affiliation definitions, id. ¶ 29, which appear to be based on indicia of "control." The current definition of affiliate extends not only to relationships involving control, but to the much more subjective test of whether relationships are such as to create an "identity of interest." 47 C.F.R. §§ 24.720(l)(1)(iv); 24.709(b)(8).

The control group and affiliation rules are complex and often cumbersome. Moreover, the control group requirements establish substantial restrictions on the ability to raise the additional capital most licensees will require to build out their systems. For example, a licensee that intends to do a public offering can ensure that the control group will continue to hold 25% of the fully diluted equity, and that no other investor or group of affiliated investors will exceed this cap, by issuing countless numbers of options to the control group, see, e.g. 47 C.F.R. § 24.709(b)(5)(i)(A). However, Pocket's investment bankers have advised that potential investors are less likely to invest in light of such automatic and immediate dilution of their investment. Moreover, it is difficult for a small business applicant or licensee to determine whether different investors might be deemed by the Commission to be "affiliated" under the Commission's rules, particularly in the case of a public offering. This is a significant burden that seems particularly unnecessary where the investors, cumulatively, would not even have de facto or de jure control.

It is typical for companies to go public while maintaining control in the hands of the principals of the company, even without specific equity and voting control caps on prospective investors. By requiring that the principals retain de jure and de facto control, and attributing the gross revenues of any investors that have such control, the Commission can continue to ensure that small business licensees remain in the hands of qualifying individuals or entities. Moreover, any such rule change should be applicable to C and F block licensees as well as future services. A rule requiring C and F block licensees to comply with the de jure and de facto control requirements, but to depart from the current attribution rules and the strict control group requirements, would facilitate efforts to raise capital and provide such licensees with a meaningful opportunity to compete in the wireless market. Moreover, if the Commission decides prospectively that the control group and attribution rules are no longer needed to ensure compliance with its general policies of promoting small business participation, there is no reason why the rules should be maintained for current licensees.

II. INSTALLMENT PAYMENTS TIED TO OPERATING CASH FLOW ARE ESSENTIAL TO SMALL BUSINESS PARTICIPATION IN THE AUCTION PROCESS.

In Paragraph 34 of the NPRM, the Commission has tentatively proposed eliminating installment payments in favor of larger bidding credits. This proposal would be devastating for small businesses. Experience in the C block (and in fact in all the designated entity auctions) has demonstrated that bidding credits are not helpful to small businesses. Bidders bid "through" the bidding credits, and, if anything, bidding credits tended to result in higher auction prices by distorting prices.

The key financial assistance that the Commission can offer to small businesses is an installment payment plan. Small start-up telecommunications businesses have no prior track record to demonstrate to potential investors. Thus, many investors hold back, waiting to see whether new, small business licensees are able to obtain service contracts, strategic investors, and success as new market entrants. An installment payment system allows small business licensees to begin making larger payments once they are cash flow positive, at which time additional financing from the capital markets will become available.[1/] Rather than abandoning installment payments, more moderate measures, such as increasing the size of the upfront payment or the down payment obligation, id. ¶ 35, may be more realistic approaches to avoiding default while facilitating participation by start-up businesses. Applicants and licensees that are able to meet these payment obligations have been able to make a threshold demonstration to

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1/ For the same reason, the Commission's tentative suggestion that bidders or auction winners be subjected to a financial screening process to qualify for installment payments, NPRM ¶ 34, would be likely to prevent many start up businesses from participating in future auctions.

lenders and investors that they have a viable business plan. They should be given an opportunity to implement those business plans in the market.

Pocket also believes that the Commission should amend its rules to create a more realistic installment payment plan for all licensees, including specifically existing C block licensees. As with more traditional financing from private capital markets, the Commission's installment plan should extend the due date of the first installment payment to the time at which small business licensees can realistically be expected to have initiated service and begun collecting revenues. In broadband PCS service, for example, given the incentive to minimize the headstart of cellular and A/B block competitors, this period would be in the range of two years after the grant of the licenses. Such a rule change would be of enormous assistance to small business licensees. It would provide a significant encouragement to the capital markets to invest in start-up telecommunications companies. And it also would give small business licensees the opportunity to use invested capital to develop their businesses into successful ventures, rather than meeting interest payment obligations. Deferred interest payments could be enhanced to reflect the time-value of money to the government while at the same time making defaults far less likely to occur. Any such rule also must apply to existing licensees, who now are struggling with the burden of paying the government debt before their markets have produced any revenue. While the Commission begins auctioning off new licenses to small businesses, it should ensure that existing small business licensees have a meaningful opportunity to become operational.

III. THE UNJUST ENRICHMENT PENALTIES SHOULD BE RATIONALIZED FOR EXISTING AND PROSPECTIVE LICENSEES.

The Commission has tentatively proposed adopting unjust enrichment rules that provide for a scale of decreasing payment liability based on the number of years the license is held. NPRM ¶ 43. This rule would be helpful to all licensees, prospectively and retroactively. A modified unjust enrichment rule still would deter license transfers that are intended to subvert the Commission's rules, but it would provide licensees with more flexibility to deal with situations of financial distress, or simply to transfer individual licenses that no longer comport with their business plans. During the early years of the license period, if transfer to a non-qualifying entity is permitted, full unjust enrichment penalties are appropriate, as the installment payments will have failed to benefit a small business, and will instead inure entirely to the non-qualifying business. However, in later years, the installment payments will have served to benefit the small business as intended. Reducing the unjust enrichment penalties on a sliding scale will permit licensees to respond to the market realities they face years out, by making more potential buyers available. The rule is therefore essential to existing licensees, and it would be unfair to deprive them of its benefits if they are made available to new licensees.

IV. THE INSTALLMENT PAYMENT AND DEFAULT RULES SHOULD NOT BE UNDULY BURDENSOME FOR LICENSEES.

A. Installment Payments

The changes to the installment payment rules proposed by the Commission would create substantial difficulties for small businesses. Many of these rules are more burdensome than those governing the C block licensees. To the extent such rules are adopted by the Commission, they should not be applied to C block licensees, who have settled financial plans and investment-backed expectations that should not be retroactively burdened.

The Commission has proposed a late payment fee for overdue installment payments. NPRM, ¶¶ 73-74. The C block rules, conversely, permit one automatic 90-day grace period for an installment payment, with no late payment fee. See, e.g., Second Report and Order, 9 FCC Rcd 2348, ¶ 240 (1994). As the experience in the C block demonstrates, licensees have utilized this automatic grace period not because they were "attempt[ing] to maximize their cash flow at the government's expense by paying late." NPRM ¶ 69. Rather, the grace period was utilized because C block licensees, in the face of current conditions in the capital markets, buildout requirements, and third party debt obligations, have simply found themselves unable to raise the capital in the compressed time frame to make those payments. At least at the outset of the license term, burdening such licensees with a late fee of up to 15% (id. ¶ 74) in a situation of financial distress only would aggravate their financial difficulties. And if such fees were due in order to obtain the grace period, as proposed in the NPRM, id., many licensees would simply be unable to pay them. Rather than making it easier for small business licensees to obtain grace periods by eliminating the need for individual showings, the late fees proposed by the Commission would in many cases make grace periods unavailable. Thus, the grace period will have failed entirely to serve its palliative purpose.

The Commission is right to seek to prevent licensees from taking advantage of favorable financing terms to benefit at the government's expense. However, in its efforts to protect against such conduct, the Commission must not lose sight of the fact that its underlying aim must be to assist small businesses, as set forth in Sections 309(j) and 257 of the Communications Act. If the balance tips too far, the losers will be bona fide small businesses that are struggling to survive in a very difficult competitive environment, and to utilize the opportunities the Commission has created. The Commission is well aware of the difficult market situation faced by start-up wireless companies, including specifically C block PCS licensees. Investment is not readily available, and the debt owed by small businesses to the government does not facilitate raising capital, as the majority of any capital raised must currently be devoted to paying interest payments. Unless the Commission is prepared to defer interest payments entirely for two or more years while licensees are given an opportunity to build out markets and attract substantial investment, it must not impose more burdensome installment payment rules.

Pocket submits however, that more stringent installment payment rules, including late fees, could be more appropriate if they were imposed after an initial period during which no installment payments were due. In this manner, once licensees were given the opportunity to gain a financially firm footing, they would be strictly required to pay in a timely manner. (As noted above, if interest payments are deferred for an initial period, as proposed, the interest rate could accordingly be increased so that the final amount paid to the government is unaffected). It is entirely reasonable to strictly enforce payment deadlines once licensees are operational.

Moreover, whether or not the grace period rules are amended, Pocket urges the Commission to take this opportunity to provide clarification regarding the confidentiality of the process existing and prospective licensees must undergo to receive extended grace periods and/or more liberal workouts. Information filed in support of a grace period or a workout necessarily will be sensitive financial information that must not be made available to third parties. The Commission's rules are silent about this issue, but they should make clear that such information is confidential, so that licensees can seek relief from the Commission without the chilling possibility that in doing so, their financial information will be disclosed to the public. In acting as a creditor, the government should provide debtor-licensees the degree of confidentiality that typically characterizes that relationship. Moreover, third parties have no legitimate interest in information concerning the debtor's financial condition or the terms of a workout between the government and a licensee.

B. Default Penalties

In those situations where a licensee is deemed in default for nonpayment of installment payments, the Commission's proposal to assess the default payment fee of Section 1.2104(g),[2] NPRM ¶ 77, would in many cases be entirely inappropriate. Licensees make installment payments for a ten-year period. While the Section 1.12104(g) penalty may be appropriate in the immediate aftermath of an auction, it becomes highly arbitrary later in the license term. And because such default penalties are well beyond those traditionally acceptable for secured creditors, they would create substantial disincentives for investors and lenders. In this scenario, the government already will have received a substantial amount of money from the licensee by the time of the default, and reauctioning the license will bring additional money into the Treasury. Moreover, the cost of the license at a reauction that is held years after the initial auction -- when market penetration is even higher and the headstart of competitors will have grown considerably -- will bear absolutely no relation to the initial auction price for that license, and it would be patently unfair to hold the initial licensee responsible for that change in market

[2] The default penalty outlined in Section 1.2104(g) is the difference between the defaulting winner's bid and the subsequent winning bid plus 3% of the lesser of these amounts.

conditions. Such a penalty also would come at the expense of other creditors junior to the Commission, and thus make it much more difficult for small businesses to raise capital. For this reason, to the extent the Commission nonetheless adopts its proposed default penalty rule, it should make clear that the rule does not apply to C block licensees. Imposing this rule on C block licensees now would unfairly burden and interfere with existing investment agreements, and could potentially undermine many financing arrangements.

A licensee that defaults once it has made good faith efforts to build out and operate its system has foregone substantial funds in the form of its upfront and down payments to the Commission. In these circumstances, default is not an appealing option, but one that may, unfortunately, be inevitable. Business plans may fail through changes in market conditions that are unforeseeable and no fault of the licensee. A licensee that has either already been offering service to the public, or that has made bona fide efforts to build out, operate, and implement a business plan endorsed by its lenders and investors, should not be penalized because it ultimately fails to succeed. Again, the Commission should not lose sight of the purpose of its rules, which are not solely to cover the costs of reauction -- but to provide small businesses with a meaningful opportunity to compete. Once the upfront and down payments have been made, the Treasury will at least have realized the cost of a reauction, if one proves necessary. If one or more installment payments have been made, the Treasury's need for the Section 1.2104(g) payment is reduced further. And the penalty will have no deterrent effect: there is no basis to believe that licensees that have paid substantial sums to the Treasury would willingly default. There is thus no basis for the penalty proposed by the Commission.

V. <u>CROSS DEFAULTS ARE NOT IN THE PUBLIC INTEREST.</u>

The Commission has sought comment on whether installment payment defaults should result in a cross default of other installment payment plan loans to the same licensee. <u>NPRM</u> ¶ 78. Pocket submits that such a rule would disserve the public interest, and should not be implemented, at least on a general basis. Such a rule most certainly should not be applied to existing licensees, as it would impose a substantial new burden on such licensees, and undermine the existing, investment-backed expectations of investors and lenders in existing licensees.[3/]

The Commission generally should be reluctant to remove licenses that are not in default. First, this would result in a decrease in service to the public and unfairly penalize a licensee who has been fulfilling the terms of its license. If one license held by a licensee fails late in the license term but the other licenses held by the licensee (whether or not in the same service) were being operated successfully, the ultimate loser in a cross-default situation would be the public, for whom competitive service would be unnecessarily interrupted. Therefore, a cross-default rule would appear to be inconsistent with the Communications Act's mandate to expedite service to the public and promote competition. <u>See</u> 47 U.S.C. § 309(j)(4).

Second, the rule is not consistent with the Commission's efforts to help small businesses. As noted above, default is not an attractive option to a licensee that has already paid substantial sums of money to the Commission in the form of an upfront and down payment (and possibly several installment payments). However, in some cases, default may be inevitable: No business plan is failproof, and licensees cannot be foresee the market conditions that ultimately may make

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[3/] Neither the existing rules nor the government Notes and Security Agreements provide for or refer to cross-default remedies.

some licenses less successful than others. Rather than deterring default, a cross-default rule would simply penalize small business licensees by linking their licenses in a manner that is significantly more onerous than that faced by their A/B block (and other) competitors, and would do so by government fiat rather than by commercially reasonable, arm's length negotiations between the lender and the debtor. The rule is especially unfair in that it would elevate a default in one market over a licensee's success in all its other markets. Thus, a business that had in most respects succeeded would never be free of the fear that it could nonetheless lose all its licenses at any time due to a failure in one isolated market. This also would make it much harder for small business licensees holding more than one license (or licenses in more than one service) to attract investors -- especially those interested in particular markets or particular services.

Third, as the Commission indicated in its Report and Order, FCC 96-278, ¶ 85 (June 24, 1996), market-oriented solutions in the event of financial distress are preferable to the Commission's reclaiming and reauctioning licenses, which would lead to investor and service disruption. The Commission's stated commitment to avoid such disruption is inconsistent with a revocation of licenses that are not in default as a remedy for default on other licenses. In general, the public interest would be better served by a rule that treated each license separately, recognizing that marketplace realities differ on a market-by-market basis, and that investors and customers in one market should not be penalized because of financial distress in a different market.

However, the Commission should reserve authority to impose a cross-default penalty on a case-by case basis, NPRM ¶ 78, on licensees that have demonstrated bad faith. Pocket believes that such authority would be sufficient to prevent defaults that occur because of bad faith or improper conduct. However, the penalty should be reserved exclusively for such situations.

CONCLUSION

For the reasons set forth above, the Commission should amend and clarify its rules to make financing more available to small business licensees and provide small businesses with a more meaningful opportunity to participate in the wireless market.

Respectfully submitted,

Lynn R. Charytan

William R. Richardson, Jr.
Lynn R. Charytan
WILMER, CUTLER & PICKERING
2445 M Street, N.W.
Washington, D.C. 20037
(202) 663-6000

Attorneys for Pocket Communications, Inc.

March 27, 1997

CERTIFICATE OF SERVICE

I, Lynn R. Charytan, hereby certify that I have this 27th day of March, 1997, caused to be hand delivered the foregoing Comments of Pocket Communications, Inc., as shown below.

Lynn R. Charytan

Michele Farquhar, Chief
Wireless Telecommunications Bureau
Federal Communications Commission
2025 M Street, N.W.
Room 5002
Washington, D.C. 20054

Jane Phillips
Wireless Telecommunications Bureau
Federal Communications Commission
2025 M Street, N.W.
Room 5202-D
Washington, DC 20054

Mark Bollinger
Wireless Telecommunications Bureau
Federal Communications Commission
2025 M Street, N.W.
Room 5604-I
Washington, D.C. 20054

Robert James
Wireless Telecommunications Burueau
Federal Communications Commission
2025 M Street, N.W.
8010-B
Washington, D.C. 20054